No. 16394

United States
COURT OF APPEALS
for the Ninth Circuit

MAYFLOWER INSURANCE EXCHANGE,

Appellant,

vs.

ROBERT DEAN GILMONT, ROSE MARIE GILMONT and RONALD A. WATSON, Guardian ad Litem for Susan Rose Gilmont, a minor, Robert Russell Gilmont, a minor and Norman I. Gilmont, a minor,

Appellees.

APPELLANT'S REPLY BRIEF

Appeal from the United States District Court for the District of Oregon.

HONORABLE WILLIAM G. EAST, District Judge.

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APPELLANT'S REPLY BRIEF

Appellant deems it necessary to briefly comment on the arguments advanced in appellees' brief. To avoid unnecessary reiteration appellant will endeavor to confine its remarks to a consideration of points which were not raised or fully developed in its opening brief.

It is readily apparent from a first reading of appellees' brief that they have failed or refused to recog-

nize the very important distinction between that kind of fraud which entitles a party to the equitable relief of rescission and that kind of fraud which is used as the basis for an action at law for the recovery of damages. This action was commenced by appellant to rescind the insurance contract and to have it declared void *ab initio* and there appears to be no disagreement on either side that this is essentially the nature of the case. Appellees in their brief (Br. 12) state "the question of fraud, misrepresentation and *rescission* should be determined by the law of the State of Oregon, * * * * *" and with this statement appellant can readily concur. Appellant cannot agree, however, that the representations which were made by McKinzie would have to have been "knowingly and wilfully made [by him] with intent to deceive or defraud the insurance company." The Oregon courts have consistently recognized the well established distinction between that fraud which raises an equitable right of rescission and that fraud which is the basis of an action for deceit for the recovery of damages.

Johnson v. Cofer, 204 Or. 142, 281 P. (2) 981 was a suit for rescission of an executed agreement whereby plaintiff conveyed a parcel of real property to defendant in exchange for certain furniture and equipment. One of the grounds of fraud relied upon by plaintiff was defendant's representation that the premises could be used for housekeeping rooms and defendant met this by asserting that plaintiff should not have relied upon this misrepresentation for the reason that they had

some prior knowledge that there had been an objection to that type of occupancy and therefore should have known better. The Oregon Supreme Court in considering this issue stated:

> "The right of rescission does not depend upon fraud intentionally or negligently committed as does an action for deceit. The contract may be vitiated either by a positive fraud actively or negligently practiced, or it may be vitiated if its consummation was accomplished through a completely innocent representation of a material fact which proved false, but was relied upon as true and except for believing in its truth the party would not have entered into the agreement." (Citing Oregon cases.)

The distinction is again recognized in *Amort v. Tupper*, 204 Or. 279, 289, 282 P. (2) 660 wherein the court stated:

> "While a court of equity follows the law, and will not permit the recovery of damages for fraud where the fraud is not consciously committed, 'whatever would be fraudulent at law will be so in equity; but the equitable doctrine goes further and includes instances of fraudulent misrepresentations which do not exist in the law.' 3 Pomeroy's Equity Jurisprudence, 5 Ed. 487, Sec. 885. For example, a court of equity will grant rescission of a contract even though there is fraud not intentionally or recklessly practiced. A completely innocent representation of a material fact, which, if false, but relied upon, and in fact accomplished a fraud, is all that is necessary." (Citing Oregon cases.)

Moreover, this court, in *Bankers Union Life Ins. Co. v. Montgomery*, 261 F. (2) 852, recognized the distinction drawn in Oregon between the necessity of showing wilful falsity with regard to answers pertaining

to physical conditions and mere falsity with respect to answers naming doctors who have treated the applicant. The reason for the distinction in Oregon is set forth in *Mutual Life Ins. Co. of N. Y. v. Chandler*, 120 Or. 694, 252 P. 559, wherein the court states:

> "The reason of this is that many times a person may be afflicted with a disease, at least in its incipient stages, without being aware thereof and may answer in good faith that he has not had any such disease. The representation, however, that he has not consulted or been treated by any other physician is one peculiarly within his knowledge and the law requires in such a case the utmost good faith and full disclosure in answer to direct inquiries on the part of one making an application for the policy."

Likewise in the instant case the information which was sought by questions in the application was peculiarly within McKinzie's own knowledge. Certainly he could not have been unaware of the fact that his license had been suspended, of the names of previous insurers, or of driving charges, citations or fines which he had received in the past three years. These statements "related to a matter forming the very basis or foundation of the contract, and worked a legal fraud on the company whether applicant intended to do so or not." *Lewis v. New York Life Ins. Co.*, 201 Mo. App. 48, 209 S.W. 625, cited in *Mutual Life Ins. Co. of N. Y. v. Chandler*, supra.

For the purpose of answering the arguments of appellees in an orderly fashion appellant will employ their subheadings.

Evidence as to Whether Application Was Delivered to McKinzie

Appellees have now raised for the first time the contention that appellant was not entitled to rely on the statements made in the application on the grounds that a copy of the application was not delivered to McKinzie. On the basis of the record in this case it is obvious that this argument is not only untenable but it comes too late.

A photostatic copy of the application was attached to the original complaint as an exhibit (R. 8); the original copy of the application bearing McKinzie's signature at the foot was introduced into evidence as Plaintiff's Exhibit 1 without objection (R. 86); the witness Snyder testified on direct examination (R. 142) and on cross examination (R. 143-144) that he delivered a copy of the application to McKinzie; and McKinzie himself testified in his deposition as follows:

> "Q. After he took the application and your money, did he give you a receipt for the money?
> A. Oh yes.
> Q. And a copy of the application?
> A. That's right.
> Q. Sometime after that did you get the policy?
> A. That's right.
> Q. Do you still have the policy?
> A. That is correct.
> Q. You still have the application?
> A. That is correct." (R. 122)

> "When a party to an action or suit stipulates or testifies deliberately to a concrete fact, not as a matter of opinion, estimate, appearance, inference, or uncertain memory, but as a considered circumstance of the case, his adversary is entitled to hold

him to it as a judicial admission. If no mistake is claimed or shown, the party so stipulating or testifying to a concrete fact cannot have the benefit of other evidence tending to falsify it. *Valdin v. Holteen and Nordstrom,* 199 Or. 135, 144, 260 P. (2) 504; Note 169 ALR 798, 800." *Morey v. Redifer,* 204 Or. 194, 214; 282 P. (2) 1062.

Evidence as to Driver's License

Appellees dwell at some length in their brief upon the matter of whether or not McKinzie had an Oregon or a California driver's license and whether or not he could have secured an Oregon driver's license at the time of the application. Whether or not McKinzie had a driver's license at the time of the application is completely beside the point for the reason that the information which was sought by the questions put to him was concerned with whether or not his license had ever been suspended or revoked. While appellees attempt to draw a distinction between the two motor vehicle driving records furnished by the Oregon Motor Vehicle Department (Ex. 7 and 35), it is nonetheless conceded by them that both of these records clearly showed that McKinzie had been suspended on February 14, 1956, and this point is admitted by appellees in their brief (Br. 15).

Assuming for the purpose of argument that prior to February 1956 McKinzie had not received any notice, or if he had received notice he had forgotten, that his Oregon driver's license had been suspended, nonetheless it is clear from his testimony that in February 1956 he applied for an Oregon driver's license and was then

advised that his driving privileges in Oregon would be suspended until February 14, 1957. McKinzie admitted that he had been so advised (R. 112) and while he may then have felt that the State of Oregon was doing him an injustice in refusing to grant him a license and in suspending his driving privileges, nonetheless he did not contend that he had forgotten this incident. To the contrary it is more likely to assume that the suspension made a distinct impression on him because he considered it a "bum rap." This was the specific information which was sought by Question 1 (c) of the application and no place in his testimony does he give any satisfactory explanation as to why he concealed this fact.

Evidence as to Driving Charges, Citations Or Fines in Past Three Years

The documentary evidence reported by the transcripts of the driving record from Oregon and California stands uncontradicted and conclusively established the misrepresentations relating to McKinzie's driving record. Appellees' attempt to weaken this evidence consists only of references to McKinzie's testimony which were taken out of context. These portions of McKinzie's testimony upon which appellees base their argument show nothing more than that when his deposition was taken he was still making clumsy efforts to evade the truth.

Evidence as to Other Claimed Misrepresentations

Appellees' brief (Br. 19) points out a mistake which appellant has made in its brief concerning the state-

ment in the application relating to automobile accidents in the past three years. Appellant admits that this was an inadvertent reference and no contention should be made that any misrepresentation was made concerning any automobile accident. Appellees are correct in bringing this matter to the attention of the court and appellant joins with them in correcting the record on this point.

Evidence Presented Jury Question

Appellees have suggested that the jury in considering its verdict "may not have believed its witnesses" (Br. 20). It should be kept in mind that the only witnesses who testified concerning the facts relevant to the issues submitted were McKinzie and the witnesses Snyder and Carlson. McKinzie admitted that he gave the answers as set forth in the application, Snyder testified that he in turn correctly put them down, and Carlson testified that if the true state of facts had been known to appellant the policy would not have been issued. There was no evidence received or offered to the contrary and if the jury didn't believe these witnesses then its verdict was based upon speculation and not on the evidence.

McKinzie made no contention that he told the truth to Snyder and that Snyder failed, for one reason or another, to put down the correct answers. The facts as presented to the jury clearly and conclusively showed that McKinzie gave false answers and in reliance on them appellant issued its policy. Under these facts appellant is clearly entitled to the relief of rescission. As

this court stated in *National Life and Accident v. Gorey,* 249 F. (2) 388:

> "As a matter of law, the evidence in this case shows that the deceased by incorrect and untrue answers misrepresented and concealed material facts; that defendant relied on such misrepresented facts, and issued its policy in reliance thereon. Because of this, the defendant's motion for a directed verdict or for a judgment n.o.v., should have been granted by the trial court." (Citations omitted)

THE TRIAL COURT ERRED IN INSTRUCTING THE JURY THAT COMMON LAW NEGLIGENCE WAS A DEFENSE

Appellees contend that appellant failed to properly object to the failure of the court to give appellant's Requested Instruction No. 2 wherein appellant requested the court to instruct the jury not to consider the defense of negligence, but tacitly admits that appellant made a proper objection to that instruction of the court wherein the court advised the jury that common law negligence on the part of the Bucholz Agency would bar a verdict in favor of appellant. The rules of this court requiring specification of error be set forth totidem verbis together with the grounds of objection urged at the trial are for the purpose of allowing this court to determine without going through the objections to the instructions page by page that the trial court was properly advised of the objection either to instructions refused or to instructions given, or a combination of both. It is possible that from a technical standpoint the objection to the failure to give appel-

lant's Requested Instruction No. 2 set forth on pages 6 and 7 of its brief should also have included the objections that appellant made to the trial court's instructing the jury that common law negligence was a defense as set forth on page 8 of appellant's brief. However, this would simply be a reiteration of the same words and it is perfectly clear from a consideration of Specification of Error 4 and 5 that the court was fully advised that appellant objected to the submission to the jury of the question of common law negligence on the part of appellant and the reasons therefor.

Appellees challenge appellant's position that the authority of the Bucholz Agency was limited to soliciting applications for insurance and accepting premium deposits, and in support thereof picked out one question and one answer from the testimony of the witness Snyder wherein he in effect stated that the Bucholz Agency was "an authorized representative of Mayflower Insurance Exchange" and totally ignored all other testimony in the case as to the limited extent of the agency. The entire testimony clearly shows that the Bucholz Agency was "an authorized representative" but that the authority was a limited one and the burden of showing otherwise was on appellees. Appellees then go on to state that conditions 19 and 22 of the insurance policy (Ex. 3) have no application in determining the question of negligence on the part of appellant as appellees are not attempting to change or waive any condition of the insurance policy. This is not correct, for, as pointed out in *Comer v. World Insurance Co.*, 212 Or. 105, 318

P. (2d) 916, under a provision comparable to condition 19 the Oregon Supreme Court stated at p. 120-121:

> "The plaintiff made no effort to prove that Dayton's authority included power to write the type of policy which he claimed he possessed; that is, one covering an applicant who, in the last five years, had received medical and hospital treatment."

In our case there is no testimony that the Bucholz Agency had authority to write a policy covering an applicant who had had his driver's license suspended and had the record of traffic violations that McKinzie did. Then appellees go on to contend that appellant itself was put on notice that there was "an ambiguity" in the answers given by McKinzie which placed it on notice to make further inquiry because applicant stated he was 40 years of age and had had no previous insurance. This is the only answer in the application (Ex. 1) which appellees contend constituted notice to appellant of irregularity and occasioned the duty to make further inquiry. Obviously, there is nothing ambiguous nor is there anything startling in the fact that the applicant had had no previous insurance carrier. A similar argument was made by the beneficiary in the case of *National Life Ins. Co. v. Gorey,* 249 F.(2d) 388 (Ninth Circuit). In that case the insured was 31 years old when he made out his application and in it he answered "none" to the question, "State names and addresses of physicians which you have ever consulted." It was there argued that the company waived the inaccurate reply by not further investigating the answer to this question on the basis that no one is in such per-

fect health as to "never have ever" consulted a physician. This court in answering this argument stated:

> "While thirty-one years of perfect health would be remarkable, the failure to consult a doctor in thirty-one years is not unheard of, nor an impossibility. Nor does such an answer imply that it must be, or is, false."

Likewise in the instant case the fact that McKinzie, at age 40, represented that he had not had his license revoked or suspended or had not had any driving charges, citations or fines in the previous three years would not be unusual, an impossibility or an implication that his answers were false. It is much more reasonable to assume that McKinzie would have given truthful answers as there would be no reason for him to misstate the facts unless he was intentionally deceiving the company for the purpose of securing an automobile liability policy.

Appellees cite as the correct rule applicable to this case one sentence from *Williams v. Pacific States Fire Co.*, 120 Or. 1, 251 P. 258, as follows:

> "The insurer will not be permitted to avoid the policy by taking advantage of any misstatement, misrepresentation or concealment, of a fact material to the risk, which is due to the mistake, fraud, negligence or other fault of its agent and not to fraud or bad faith on the part of the insured:"

As far as the above quotation is concerned it may be under certain circumstances a correct statement of a rule of law but this one sentence taken out of context has no application to the facts in this case. In the Wil-

liams case there was no controversy as to the fact that the prospective assured had orally given the correct information requested by the agent. There was no application form signed by the prospective assured and the "agent" in procuring the insurance policy gave incorrect information to the issuing company. The assured never saw the policy and had no knowledge of the false statements made by the "agent" to induce the issuance of the policy in question until after the loss. When the assured brought action on the policy the insurance company set up as a defense the false statements made by the "agent" to induce the issuance of the policy. The assured then contended that the insurance company was estopped from claiming the false representations contained in the policy would render the policy void because any error or oversight in making these representations was made by its agent. The main controversy then resolved itself into whether the "agent" was the agent for the assured or the agent for the insurance company, and the jury resolved this question in favor of the assured. This case was therefore decided on the doctrine of estoppel *in pais* which prevented the insurance company from disproving the truth of the statements made by its authorized agent in making up the application for insurance.

> "The defendant company is estopped from claiming that any error or oversight of A. D. Trunkey, or Lamping & Company, acting as its agent, in making the representations or warranties contained in the policy, would render the policy void. A contrary holding would open wide the door to fraud and permit an insurer by having its agent

> insert in a policy of insurance erroneous statements without the knowledge or assent of the assured to collect the premiums and render it optional with the insurance company to pay any loss occurring. The law does not sanction such a rule." (P. 10)

The distinction between the rule which applies where the agent through mistake, fraud, negligence or other fault makes a misstatement in the application unknown to the prospective assured and the rule where the applicant gives the agent a false statement of the facts which the agent correctly sets forth in the application form is recognized in *Tri-State Ins. Co. v. Ford*, 120 F. Supp. 118, which case incidentally answers nearly every contention raised by appellees. In the Tri-State case the policy in question contained provisions identical with those contained in Exhibit 3. The false representation was that no policy of insurance had been cancelled during the previous year. The court found that the insurance company did not discover that this statement was false until after an accident, that the local soliciting agent was guilty of negligence in not verifying the truthfulness of this representation since he knew facts that should have put him upon inquiry, namely, that the applicant had come all the way from another town to do business and the agent had read a letter from the prospective mortgagee, also to be covered by the policy for loss by collision, to the applicant stating that its file showed the collision coverage had been cancelled by an insurance company. At p. 122 the court stated:

> "The plaintiff company, on whom the fraud was practiced, had no *actual* knowledge of the mis-

representation and cannot be deemed to have waived this material risk element and to have knowingly entered into the contractual arrangement. Although, admittedly the plaintiff's soliciting agent had facts which upon inquiry would have revealed the truth the plaintiff company cannot be bound by the agent's failure to inquire inasmuch as this soliciting agent was not clothed with ostensible authority to waive a matter so material to the risk, even if said agent had possessed *actual* and not merely *constructive* notice himself. The insured cannot be purged from his own fraud upon the rationale that the plaintiff thhrough its soliciting agent engaged in conduct which in legal fiction amounted to a waiver of a material warranty by the insured *when the agent accepted* the premium payments. The case at bar must be sharply distinguished from those lines of cases wherein the agent of the insurer in order to write the policy either mistakenly or fraudulently fills in an insurance application warranty when the warranted representation material to the risk was in fact truly and accurately stated by the prospective insured. Obviously, where the applicant in the utmost of good faith truthfully states all facts pertinent to inquiry and pays his premium with the understanding that the policy has been accepted by the insurer, any negligent or fraudulent conduct on the part of the agent must be imputed to the insurance company and not to the insured."

In *Comer v. World Ins. Co.*, supra, we have the same situation as in *Williams v. Pacific States Fire Co.*, supra, namely, the agent in an application form for a policy of health and disability insurance wrote down words relative to the prior physical condition of the applicant which were false. The assured sued on the policy, the insurance company pleaded as a defense the

false representations made in the application, and the assured then contended that the insurance company was estopped to resort to the truth in defending itself because (1) the assured had told the agent the truth about his illness; (2) the agent made false entries in the application form without the assured's knowledge; (3) the insurance company delivered the policy to the assured as a valid contract of insurance; and (4) the assured paid the premiums in good faith and relied upon the policy. The verdict was for the plaintiff-assured and on appeal the Oregon Supreme Court held that in the light of ORS 736.305 (quoted in full in appellees' brief p. 5), the pertinent portion of which is set forth for convenience as follows:

> "Every contract of insurance shall be construed according to the terms and conditions of the policy, except where the contract is made pursuant to a written application therefor, and such written application is intended to be made a part of the insurance contract. In that case, if the company delivers a copy of such application to the assured, thereupon such application shall become a part of the insurance contract. If the application is not so delivered to the assured, it shall not be made a part of the insurance contract."

the plaintiff-assured was charged with knowledge of the contents of the application and there was no basis for the equitable estoppel which the assured sought to invoke. "To the contrary, it showed that the policy was obtained by false representations and that the defendant's motion for a directed verdict should have been sustained." (P. 131) There was a concurring opinion in which the minority held that the decision was cor-

rect either on the ground that there was no pleading of estoppel or that the assured had admitted that he did give at least one false answer to the agent, but disagreed with the majority holding that the assured was bound by the false declarations even though he claimed that he was not aware thereof, as according to the minority this was in effect holding that the assured was guilty of fraud even though he might not have known that the answers on the application were false. The important point is that the defense of estoppel based on the fraud, mistake or negligence of the agent in preparing the application form could not be asserted by the assured where a copy of the application was furnished the assured, as in our case, according to the majority opinion, while the minority opinion would limit estoppel to those cases where the agent by fraud, mistake or negligence incorrectly wrote down the answers and the applicant did not know of the false answers. It may be argued that a distinction should be made between the cases where the "negligence" of the agent was in incorrectly writing down the answers and those cases in which the insurance company had actual knowledge of a situation which would put it on notice that the answers given were false, but this seems to appellant a distinction without a difference, and in the absence of actual knowledge by the insurance company would allow the wrongdoer to profit by his own wrong. In any event, common law negligence is not a proper defense and the instruction of the court cannot be tortured into an instruction dealing with estoppel *in pais*. Further, appellees are up against a stone wall in at-

tempting to profit by McKinzie's fraud. See *Johnson v.* Cofer, 204 Or. 142, 281 P.(2d) 981, where in an equitable action for rescission the court stated at p. 149:

> "It is a well established principle of law that in order to secure relief on the ground of fraud, the person claiming reliance must have had a right to rely upon the representations. Generally speaking, the right to rely on representations presents the question of the duty of the party to whom the representations have been made to use diligence in respect to those representations. The courts are not entirely in accord as to the necessity of diligence at all where fraud has been employed, especially where representations are of a positive nature. 'The policy of the courts is, on the one hand, to suppress fraud and, on the other, not to encourage negligence and inattention to one's own interests. The rule of law is one of policy. Is it better to encourage negligence in the foolish, or fraud in the deceitful? Either course has obvious dangers. But judicial experience exemplifies that the former is the less objectionable and hampers less the administration of pure justice. The law is not designed to protect the vigilant, or tolerably vigilant, alone, although it rather favors them, but is intended as a protection to even the foolishly credulous, as against the machinations of the designedly wicked. It has also been frequently declared that as between the original parties, one who has intentionally deceived the other to his prejudice is not to be heard to say, in defense of the charge of fraud, that the innocent party ought not to have trusted him or was guilty of negligence in so doing.' 23 Am. Jur. 948, Fraud and Deceit, Sec. 146. See also *Larsen et al. v. Lootens et al.,* 102 Or. 579, 194 P. 699, 203 P. 621."

In further support of their contention that the instruction on common law negligence was proper ap-

pellees cite *Elliott v. Mork*, 144 Or. 246, 24 P.(2d) 1036. This case states a rule of limited application, namely, in relation to the sale or exchange of real property, and is not pertinent to our inquiry, for, as stated in *Tri-State Ins. Co. v. Ford*, supra, at p. 122:

> "Although there is a rule, applicable particularly in the law of sales, that where the one on whom the alleged fraud was perpetrated, knew or could have known of the fraud, said person cannot urge the misrepresentation in order to vitiate the contract between the parties, such rule has no application in the instant case."

Appellant again reiterates that it was entitled to a directed verdict, having conclusively proved all elements entitling it to rescind the insurance contract, and further that in the event this court is of a contrary opinion that appellant is certainly entitled to a new trial because of the erroneous instruction relative to common law negligence.

Respectfully submitted,

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